

Message Text

CONFIDENTIAL

PAGE 01 OECD P 06420 01 OF 06 041219Z
ACTION EUR-12

INFO OCT-01 ISO-00 AID-05 CEA-01 CIAE-00 COME-00 EB-08
EA-07 FRB-03 INR-07 IO-13 NEA-10 NSAE-00 OPIC-03
SP-02 TRSE-00 LAB-04 SIL-01 AGRE-00 OMB-01 SSO-00
INRE-00 USIE-00 NSC-05 SS-15 STR-04 NSCE-00 EURE-00
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O R 041140Z MAR 77
FM USMISSION OECD PARIS
TO SECSTATE WASH DC IMMEDIATE 5571
INFO ALL OECD CAPITALS 0724

C O N F I D E N T I A L SECTION 01 OF 06 OECD PARIS 06420

PASS TREASURY, FEDERAL RESERVE, CEA

E.O. 11652: GDS
TAGS: EFIN, ECON, OECD
SUBJECT: EPC'S WORKING PARTY 3 MEETING OF FEB. 28, 1977

REF: (A) CPE/WP3(77)1, (B) CPE/WP3(77)2,
(C) OECD PARIS 5945

1. SUMMARY. ONE-DAY MEETING OF WP3 ON FEBRUARY 28
FOCUSSED ON (A) MEDIUM-TERM CURRENT ACCOUNT PROSPECTS
AND PROBLEMS OF ADJUSTMENT AND (B) 1977 CURRENT ACCOUNT
AND ADJUSTMENT PROSPECTS. WHILE A NUMBER OF DELEGATIONS
EXPRESSED VARYING DEGREES OF SKEPTICISM REGARDING METH-
ODOLOGY AND POLICY IMPLICATIONS OF THE SECRETARIAT'S
PROPOSED EXERCISE ON FUTURE PATTERN OF CURRENT ACCOUNT
BALANCES, WORKING PARTY ACCEPTED THE SECRETARIAT'S REC-
COMMENDATION TO HAVE GROUP OF EXPERTS STUDY THIS ISSUE IN
MORE DETAIL. THE MANDATE FOR SUCH A FURTHER EXAMINATION,
HOWEVER, WAS MODIFIED AS NOTED BELOW FROM THAT SUGGESTED
IN PARAGRAPH 8 OF REFD0C B. DISCUSSION OF MEDIUM- AND
SHORT-TERM CURRENT ACCOUNT PROSPECTS DREW ATTENTION TO
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PAGE 02 OECD P 06420 01 OF 06 041219Z

THE PROBABLE PERSISTENCE OF LARGE DEFICITS IN MANY OF
THE SMALLER OECD COUNTRIES. THE REVIEW OF SHORT-TERM
CURRENT ACCOUNT PROSPECTS IDENTIFIED SEVERAL DIFFERENCES
BETWEEN SECRETARIAT AND COUNTRY FORECASTS: FRANCE SUB-
MITTED ESTIMATES OF LOWER DEFICITS FOR 1976 AND 1977;
GERMANY AND SWITZERLAND FORESEE SMALLER SURPLUSES; ITALY
NOTED A SMALLER DEFICIT FOR 1976; SWEDEN REPORTED LARGER

DEFICITS FOR 1976 AND 1977; AND US EXPECTS A SOMEWHAT LARGER DEFICIT IN 1977. DISCUSSION OF SHORT-TERM PROSPECTS SUGGESTED THAT THE ADJUSTMENT PROCESS WAS WORKING IN THE RIGHT DIRECTION, ALBEIT SLOWLY, AND THAT NO SERIOUS FINANCING PROBLEMS WERE FORESEEN FOR 1977, EXCEPT FOR TWO OR THREE OF THE SMALLER OECD COUNTRIES. NO DATE FOR NEXT MEETING OF WP3 WAS SET. A MEETING BEFORE APRIL 28-29 INTERIM COMMITTEE MEETING IN WASHINGTON IS UNDER CONSIDERATION. END SUMMARY

MEDIUM-TERM PATTERN OF CURRENT ACCOUNTS AND ADJUSTMENT PROCESS

2. CHAIRMAN EMMINGER AND FAY (SECRETARIAT) STRESSED THAT FIGURES IN THE SECRETARIAT'S DOCUMENTATION (THE "REFERENCE CASE") WERE TO BE CONSTRUED AS PROJECTIONS BASED ON SPECIFIC ASSUMPTIONS, NOT FORECASTS. INCLUSION OF CAPITAL FLOWS IN THE ANALYSIS WAS COMMENDED BY A NUMBER OF DELEGATIONS. THE GENERAL APPROACH PRESENTED BY THE SECRETARIAT MET WITH VARYING DEGREES OF SKEPTICISM. EMMINGER CALLED ATTENTION TO LACK OF REALITY RESULTING FROM ASSUMPTION OF UNCHANGED EXCHANGE RATES AND EXPRESSED CONCERN FIGURES WOULD BE MISUSED. MOST REPRESENTATIVES CAUTIONED AGAINST DRAWING POLICY CONCLUSIONS FROM NUMERICAL RESULTS DERIVED FROM THE EXERCISE. US, FRENCH AND JAPANESE DELEGATIONS WERE MOST CRITICAL OF THE UNDERLYING METHODOLOGY AND OF SOME OF THE POLICY IMPLICATIONS. UK, SWISS, BELGIAN, ITALIAN, AND CANADIAN DELEGATIONS VOICED SUPPORT FOR THE SECRETARIAT'S APPROACH, ALTHOUGH CONFIDENTIAL

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PAGE 03 OECD P 06420 01 OF 06 041219Z

EVEN THE UNITED KINGDOM (MITCHELL), THE STRONGEST PROPONENT FOR AN EXPERTS GROUP ON

CONFIDENTIAL

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PAGE 01 OECD P 06420 02 OF 06 041220Z
ACTION EUR-12

INFO OCT-01 ISO-00 AID-05 CEA-01 CIAE-00 COME-00 EB-08

EA-07 FRB-03 INR-07 IO-13 NEA-10 NSAE-00 OPIC-03
SP-02 TRSE-00 LAB-04 SIL-01 AGRE-00 OMB-01 SSO-00
INRE-00 USIE-00 NSC-05 SS-15 STR-04 NSCE-00 EURE-00
/102 W

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FM USMISSION OECD PARIS

TO SECSTATE WASH DC IMMEDIATE 5572

INFO ALL OECD CAPITALS 0725

C O N F I D E N T I A L SECTION 02 OF 06 OECD PARIS 06420

THIS SUBJECT (SEE BELOW), QUESTIONED SOME OF THE ANALYSIS.

3. US DEL (PARTEE) NOTED THAT ALL FORECASTING EXERCISES ARE SUBJECT TO UNANTICIPATED CHANGES IN VARIABLES INFLUENCING THE FORECAST. SUCH CHANGES COULD HAVE DRAMATIC EFFECTS ON FORECASTS OF A VARIABLE SUCH AS THE CURRENT ACCOUNT, ESPECIALLY SINCE THIS IS A RESIDUAL ITEM AND SINCE IT IS AFFECTED BY CHANGING DEVELOPMENTS IN THE DOMESTIC ECONOMY. MOREOVER, CHANGES IN SUCH PRICE PARAMETERS AS EXCHANGE RATES (THAT ARE ASSUMED NOT TO CHANGE IN THE SECRETARIAT'S EXERCISE) AND INTEREST RATES COULD RADICALLY AFFECT CURRENT ACCOUNT AND CAPITAL ACCOUNT FORECASTS. US (WIDMAN) OBSERVED THAT WHILE PRINCIPLE OF FORECASTING AS AID TO POLICY FORMULATION WAS FULLY ACCEPTED, THE EXERCISE WAS SUBJECT TO SERIOUS TECHNICAL PROBLEMS. MARGINS OF ERROR AND ACCEPTABILITY OF NUMEROUS DIVERGENT PATTERNS WOULD LIMIT OPERATIONAL UTILITY, AND THERE WAS DANGER RESULTS WOULD BE USED IMPROPERLY. HE FELT WP COULD CONCLUDE ON A JUDGMENTAL BASIS, WITHOUT CONFIDENTIAL

CONFIDENTIAL

PAGE 02 OECD P 06420 02 OF 06 041220Z

UNDERTAKING PROJECTION EXERCISE, THAT THERE IS A SERIOUS PROBLEM IN THE MALDISTRIBUTION OF PAYMENTS POSITIONS. WP COULD PROBABLY AGREE ON DESIRED DIRECTION OF CHANGE IN POSITIONS OF INDIVIDUAL COUNTRIES AND ON JUDGMENT THAT CHANGE SHOULD BE SUBSTANTIAL AND PROMPT. US (JUNZ) ADDED THAT THE QUESTION OF DETERMINING AN UNDERLYING CURRENT ACCOUNT PATTERN HAS BEEN DISCUSSED ON VARIOUS OCCASIONS. AT LAST YEAR'S MEETING ON THIS ISSUE, SPONSORED BY THE IMF, IT HAD BEEN CONCLUDED THAT THE STATE OF THE ART ON THIS SUBJECT HAD NOT IMPROVED. THE ADJUSTMENT PROCESS IS DYNAMIC; THE SECRETARIAT'S METHODOLOGY, ON THE OTHER HAND, IS STATIC IN CHARACTER. TO ACHIEVE EFFECTIVE ADJUSTMENT, TRADE ELASTICITIES MUST CHANGE, SO THAT IT IS ANALYTICALLY INAPPROPRIATE TO DRAW ON HISTORICAL ELASTI-

CITIES, AS SECRETARIAT HAS DONE, TO MAKE PROJECTIONS FOR 1979.

4. FRANCE (BAQUIAST) FOUND THE SECRETARIAT APPROACH "TOO COMPLETE", AND CONSIDERED THE EXERCISE MORE ACADEMIC THAN OPERATIONAL. THERE WERE TOO MANY UNCERTAINTIES RELATED TO THE NUMEROUS VARIABLES ENTERING THIS SORT OF ANALYSIS, PARTICULARLY WITH REGARD TO THE PRICE OF OPEC OIL AND OPEC INVESTMENT DECISIONS, TO MAKE THE EXERCISE USEFUL. ATTACHING PRECISE NUMBERS TO INDIVIDUAL COUNTRIES COULD BE DANGEROUS; CIRCULATION OF THESE SORTS OF NUMBERS TO THE PUBLIC COULD ALARM PUBLIC OPINION. NEVERTHELESS, FRENCH DEL (DE LAROSIERE) SUBSEQUENTLY CITED THE RESULTS OF THE EXERCISE HE HAD FOUND UNACCEPTABLE AS EVIDENCE THAT PROSPECTIVE SHIFTS IN THE DISTRIBUTION WOULD LEAVE SOME COUNTRIES BEARING DISPROPORTIONATE SHARE OF REMAINING OVERALL OECD DEFICIT. NAMELY, EXACERBATION OF THE IMBALANCE BY MOVEMENTS IN ONE GROUP OF STRONG COUNTRIES (E.G. LARGER SURPLUS FOR JAPAN) WOULD OFFSET CONTRIBUTION TO REDUCTION OF IMBALANCE BY A SECOND GROUP (E.G., SMALLER DEFICITS FOR UK AND ITALY, LARGER DEFICIT FOR US), SO THAT A THIRD GROUP WHOSE DEFICITS REMAINED CONFIDENTIAL

CONFIDENTIAL

PAGE 03 OECD P 06420 02 OF 06 041220Z

RELATIVELY STAGNANT (FRANCE AND SMALLER COUNTRIES) WOULD EMERGE WITH UNACCEPTABLY LARGE SHARE OF DEFICIT.

5. JAPAN (MATSUKAWA) QUESTIONED THE APPROPRIATENESS OF THE SECRETARIAT'S ASSUMPTIONS, PARTICULARLY AS THEY APPLIED TO JAPAN. IT WAS MOST UNLIKELY THAT JAPAN WOULD INCUR THE \$9 BILLION CURRENT ACCOUNT SURPLUS IN 1979 WHICH THE SECRETARIAT EXERCISE CONTEMPLATES. SMALL CHANGES IN THE SECRETARIAT'S ASSUMPTIONS WOULD RESULT IN VERY DIFFERENT RESULTS. (FOR EXAMPLE, USING THE SECOND HALF OF 1976 AS A BASE RATHER THAN THE FULL YEAR 1976 AND USING IMPORT/EXPORT ELASTICITIES FOR THE OECD REGION FOR JAPAN RATHER THAN THE ONES USED IN THE "REFERENCE CASE" WOULD ELIMINATE MOST OF THE \$9 BILLION SURPLUS PROJECTED BY THE SECRETARIAT EVEN IF THE OTHER ASSUMPTIONS USED BY THE SECRETARIAT WERE RETAINED.)

6. EMMINGER CONCLUDED THIS PART OF DISCUSSION BY NOTING THAT NUMBERS DERIVED FROM THIS EXERCISE MAY LEAVE FALSE IMPRESSION OF PRECISION. VALUE OF EXERCISE WOULD BE IN IDENTIFYING LIKELY TRENDS AND TENDENCIES, AND ONE MUST BE CAUTIOUS NOT TO DRAW POLICY IMPLICATIONS BASED SOLELY ON THIS SORT OF ANALYSIS.

7. MITCHELL AND WIDMAN NOTED THAT SECRETARIAT MAY BE UNDERSTATING SIZE OF OPEC SURPLUS OVER NEXT THREE YEARS,

AND THEREFORE MAY BE UNDERSTATING ORDER OF MAGNITUDE OF
MEDIUM-TERM ADJUSTMENT AND FINANCING PROBLEMS. SEVERAL

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PAGE 01 OECD P 06420 03 OF 06 041229Z
ACTION EUR-12

INFO OCT-01 ISO-00 AID-05 CEA-01 CIAE-00 COME-00 EB-08
EA-07 FRB-03 INR-07 IO-13 NEA-10 NSAE-00 OPIC-03
SP-02 TRSE-00 LAB-04 SIL-01 AGRE-00 OMB-01 SSO-00
INRE-00 USIE-00 NSC-05 SS-15 STR-04 EURE-00 /102 W
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O R 041140Z MAR 77
FM USMISSION OECD PARIS
TO SECSTATE WASH DC IMMEDIATE 5573
INFO ALL OECD CAPITALS 0726

C O N F I D E N T I A L SECTION 03 OF 06 OECD PARIS 06420

REPRESENTATIVES INDICATED THAT VIEWING DISTRIBUTION OF
CURRENT ACCOUNT DEFICITS BY COUNTRY GROUPINGS MAY LEAD
TO MISLEADING RESULTS. WIDMAN CAUTIONED AGAINST GENERAL-
IZATIONS MADE BY SEVERAL DELEGATES ABOUT DIFFICULTIES OF
DEVELOPING COUNTRIES AS A GROUP, INDICATING IT WAS NECES-
SARY TO DISAGGREGATE. FOR EXAMPLE, HE NOTED THAT TWO
COUNTRIES ACCOUNT FOR NEARLY HALF OF THE DEFICIT OF THE
GROUP OF NON-OIL DEVELOPING COUNTRIES. SUCCESS IN THE
ADJUSTMENT MEASURES THESE TWO COUNTRIES HAVE BEEN RE-
QUIRED TO TAKE WOULD THEREFORE LOWER THE DEFICIT FORE-
SEEN BY THE SECRETARIAT FOR THIS GROUP, AND IT WOULD BE
WRONG TO CONCLUDE THAT ALL LDC'S FACE EQUALLY SEVERE
FINANCIAL PROBLEMS. LAMFALUSSY (BIS) NOTED THAT SINCE
SOME OF THE OPEC MEMBERS ARE CURRENT AND PROSPECTIVE
BORROWERS, REFERENCE TO A GLOBAL OPEC SURPLUS UNDERSTATES
THE SIZE OF GLOBAL FINANCING NEEDS FOR THE OPEC AND NON-
OPEC COUNTRIES IN BOTH THE NEAR- AND MEDIUM-TERM.

8. WITH REGARD TO POLICY CHOICES TO DEAL WITH THE CUR-
RENT ACCOUNT DISTRIBUTION PROBLEM, MITCHELL INDICATED
THAT TRADE RESTRICTIONS AND FURTHER DEFLATION BY COUN-
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PAGE 02 OECD P 06420 03 OF 06 041229Z

TRIES IN DEFICIT WERE NOT TO BE RECOMMENDED; ADJUSTMENT VIA MORE RAPID EXPANSION BY COUNTRIES IN SURPLUS AND CHANGES IN REAL EXCHANGE RATES WOULD BE BY FAR THE PREFERABLE COURSE. COUNTRIES IN SURPLUS SHOULD NOT STAND IN WAY OF NECESSARY EXCHANGE-RATE CHANGES. FRANCE (DE LAROSIERE), SWITZERLAND (LANGUETIN), BELGIUM (JANSON) AND SWEDEN (WOHLIN) EXPRESSED RESERVATIONS ABOUT RELYING ON EXCHANGE-RATES AS AN INSTRUMENT FOR DEALING WITH REDISTRIBUTION OF BALANCES; RATHER, DOMESTIC POLICIES DEALING WITH UNDERLYING CONDITIONS SHOULD BE THE PRIMARY MEANS OF ADJUSTMENT.

9. WIDMAN TOOK VIEW THAT NEED FOR REDUCING CURRENT ACCOUNT DEFICITS WAS RELATED TO ABILITY TO ATTRACT PRIVATE CAPITAL. IF COUNTRIES WERE PURSUING POLICIES WHICH WILL HOLD CONFIDENCE OF PRIVATE LENDERS, THEY COULD CONTINUE TO RUN DEFICITS. RESTRICTIVE DEMAND MANAGEMENT POLICIES WOULD BE ESSENTIAL IN DEALING WITH DOMESTIC INFLATION. HOWEVER, FROM EXTERNAL PAYMENTS STANDPOINT BASIC NEED OF WEAKER COUNTRIES WAS TO RESTRUCTURE THEIR ECONOMIES AND SHIFT RESOURCES TO THE INVESTMENT AND EXPORT SECTORS SO THAT GROWTH WOULD NOT BE INCOMPATIBLE WITH REGAINING EXTERNAL STABILITY. FINANCIAL ASSISTANCE FROM THE INTERNATIONAL COMMUNITY TO COUNTRIES THAT ARE PURSUING THIS PATH MAY BE APPROPRIATE IN SOME CASES TO ASSIST AND ENCOURAGE SUCH RESTRUCTURING. COUNTRIES IN SURPLUS ALSO HAVE RESPONSIBILITY TO EXPAND ECONOMIES AS RAPIDLY AS CONSISTENT WITH SUSTAINED GROWTH AND AVOIDING RESURGENCE OF INFLATION. CANADA (HOOD) ASSOCIATED ITSELF WITH LATTER POINT, AND ADDED THAT SINCE SOURCE OF DEFICIT IN MANY CASES IS INFLATION, COUNTRIES IN DEFICIT MUST GET INFLATION UNDER CONTROL. WOHLIN OBSERVED THAT MORE RAPID GROWTH BY COUNTRIES IN SURPLUS MAY NOT NECESSARILY BENEFIT THE COUNTRIES IN DEFICIT IF SUCH EXPANSION IS ORIENTED TO INVESTMENT IN EXPORT SECTORS THAT INCREASES THE COMPETITIVENESS OF COUNTRIES IN SURPLUS. MORE RAPID

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CONFIDENTIAL

PAGE 03 OECD P 06420 03 OF 06 041229Z

ECONOMIC GROWTH BY THE COUNTRIES IN SURPLUS SHOULD THEREFORE BE CONSUMPTION-LED, THEREBY SUCKING IN IMPORTS.

10. A NUMBER OF REPRESENTATIVES STRESSED FEAR THAT INDIVIDUAL COUNTRIES--PARTICULARLY THE SMALLER ONES AND THE NON-OIL DEVELOPING COUNTRIES--MAY BE FACING INCREASING DIFFICULTIES IN OBTAINING CONTINUED FINANCING FROM

THE BANKING COMMUNITY. PARTEE NOTED THAT THE LARGE US BANKS ARE BECOMING INCREASINGLY CONCERNED ABOUT RISK EXPOSURE IN PARTICULAR COUNTRY ENVIRONMENTS. SEVERAL REPRESENTATIVES--KESSLER (THE NETHERLANDS), WOHLIN AND MITCHELL--URGED THE SECRETARIAT TO ASSEMBLE MORE DATA ON DEBT BURDENS OF INDIVIDUAL COUNTRIES.

GROUP OF EXPERTS PROPOSAL

11. THE SECRETARIAT'S PROPOSAL TO ESTABLISH A GROUP OF EXPERTS TO CONSIDER IN MORE DETAIL THE METHODOLOGY AND RESULTS OF THE SECRETARIAT'S ANALYSIS WAS DISCUSSED BY THE WORKING PARTY. PARTEE, IN SUPPORTING ESTABLISHING SUCH A GROUP, URGED THAT THE GROUP LOOK AT THE ASSUMPTIONS MORE CAREFULLY, PERHAPS LOOSENING UP ON THE ASSUMPTIONS WITH REGARD TO EXCHANGE-RATES AND THE CAPITAL ACCOUNT, AND HE SUGGESTED THAT EXPERTS GROUP DRAW ON COUNTRY INPUT AND REPORT BACK TO WP3 DIRECTLY RATHER THAN TO SECRETARIAT. MATSUKAWA URGED THAT EXPERTS GROUP NOT PRESENT SINGLE SET OF NUMBERS BUT RATHER SEVERAL SETS

CONFIDENTIAL

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PAGE 01 OECD P 06420 04 OF 06 041314Z
ACTION EUR-12

INFO OCT-01 ISO-00 AID-05 CEA-01 CIAE-00 COME-00 EB-08
EA-07 FRB-03 INR-07 IO-13 NEA-10 NSAE-00 OPIC-03
SP-02 TRSE-00 LAB-04 SIL-01 AGRE-00 OMB-01 SSO-00
INRE-00 USIE-00 NSC-05 SS-15 STR-04 NSCE-00 EURE-00
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O R 041140Z MAR 77
FM USMISSION OECD PARIS
TO SECSTATE WASH DC IMMEDIATE 5574
INFO ALL OECD CAPITALS 0727

C O N F I D E N T I A L SECTION 04 OF 06 OECD PARIS 06420

BASED ON DIFFERENT ASSUMPTIONS, AND THAT THE ASSUMPTIONS USED BE ASSESSED BY NATIONAL GOVERNMENTS. MITCHELL'S SENSE OF URGENCY THAT EXPERTS GROUP MEET SOON AND BE READY TO REPORT TO WP3 BEFORE APRIL MEETING OF INTERIM COMMITTEE WAS NOT SHARED BY OTHER DELEGATIONS. FAY NOTED

THAT WHAT SECRETARIAT HAD IN MIND WITH EXPERTS GROUP WAS NOT A PURELY TECHNICAL EXERCISE BUT TO DRAW ON SENIOR STAFF OF COUNTRIES TO HELP SECRETARIAT IN FORMULATING GENERAL LINES OF EXERCISE. HE THOUGHT ONE MEETING ON THE FRAMEWORK OF THE EXERCISE, EMPHASIZING WHAT WOULD BE MOST USEFUL TO MEMBER COUNTRIES, WOULD BE SUFFICIENT. SECRETARIAT THEN WOULD CONTACT NATIONAL GOVERNMENTS AND HAVE TECHNICAL CONSULTATIONS ABOUT ELASTICITIES. EMMINGER CONCLUDED THAT A MEETING OF EXPERTS SHOULD BE CONVENED, PERHAPS IN FOUR WEEKS OR SO. GROUP COULD CONSIDER ALTERNATIVE PROJECTIONS AND GIVE MORE REGARD TO ASSUMPTIONS AND FEASIBILITY QUESTIONS OF VARIOUS DELEGATIONS, AND REPORT BACK TO WORKING PARTY. FAY NOTED THAT SECRETARIAT COULD NOT REWORK PAPER WITHIN SHORT PERIOD, AND ANY SUBSTANTIAL REVISIONS OR RECOMMENDATION BY EXPERTS GROUP WOULD DELAY REPORT (TO SUBSEQUENT WP MEETING) FOR AT LEAST SEVERAL WEEKS.

CONFIDENTIAL

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PAGE 02 OECD P 06420 04 OF 06 041314Z

SHORT-TERM CURRENT ACCOUNT OUTLOOK

12. SCHWARTZ (IMF) SUMMARIED LATEST IMF WORLD ECONOMIC OUTLOOK PAPER. WHILE PRINCIPALLY IN BROAD AGREEMENT WITH SECRETARIAT'S ASSESSMENT OF OUTLOOK, IMF DOES FORESEE A SOMEWHAT STRONGER GROWTH IN OUTPUT FOR INDUSTRIAL COUNTRIES AND A CONSIDERABLY LARGER GROWTH IN VOLUME OF TRADE IN 1977 FOR INDUSTRIAL COUNTRIES, ESPECIALLY FOR EXPORTS (8 PERCENT VERSUS 6 PERCENT BY SECRETARIAT). THE IMF PAPER ON ADJUSTMENT PROCESS RELIES ON JUDGMENTAL ASSESSMENT OF PAYMENTS PROSPECTS FOR GROUPS OF COUNTRIES RATHER THAN ON FORMALLY-DERIVED PAYMENTS NUMBERS.

13. IN REVIEW OF 1977 CURRENT ACCOUNT PROSPECTS, SEVERAL COUNTRIES PRESENTED FORECASTS THAT DIFFERED FROM THOSE PRESENTED IN TABLE 1 OF REFDOC A. GERMANY (WEBER) CITED A FORECAST OF \$2 TO 3 BILLION SURPLUS INSTEAD OF SECRETARIAT'S \$4-1/2 BILLION. WEBER PRESENTED AN ELABORATE SET OF NUMBERS TO SUPPORT THE GERMAN CONTENTION THAT FRG HAS BEEN SHARING IN THE ADJUSTMENT PROCESS SINCE IMPORT GROWTH HAS RECENTLY BEEN QUITE ELASTIC RELATIVE TO GROWTH OF DOMESTIC DEMAND--SIGNIFICANTLY MORE SO THAN IN OTHER COUNTRIES. DE LAROSIERE CITED ESTIMATED DEFICIT FOR 1976 OF \$5-1/2 BILLION (COMPARED WITH 6-1/2 FIGURE BY SECRETARIAT) AND LATEST GOVERNMENT FORECAST FOR 1977 EXCEEDING 3-1/2 (COMPARED WITH SECRETARIAT'S 4-1/2). DE LAROSIERE NOTED THAT ELEMENTS EXPLAINING SWING FROM NEAR BALANCE TO \$5-1/2 BILLION DEFICIT IN 1976 INCLUDE: (A) \$1 BILLION DUE TO DROUGHT, (B) \$2 BILLION DUE TO INCREASE IN PRICE OF OIL IMPORTS, REFLECTING DEPRECIATION.

TION OF FRANC; AND (C) \$1 BILLION DUE TO INCREASE IN VOLUME OF OIL IMPORTS. HE NOTED THAT DEPRECIATION OF FRANC HAS LED TO DETERIORATION OF TRADE BALANCE--J-CURVE EFFECT ACTING ON IMPORTS--AND ADDED THAT UPWARD PART OF J-CURVE MAY NOT MATERIALIZE, SINCE FRENCH EXPORTERS HAVE
CONFIDENTIAL

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PAGE 03 OECD P 06420 04 OF 06 041314Z

RIASED PRICES. LANGUETIN CLAIMED THAT SECRETARIAT'S 1977 FORECAST FOR SWISS SURPLUS OF \$4 BILLION IS EXAGGERATED, BUT HE DID NOT PRESENT A GOVERNMENT ESTIMATE. ITALY (IZZO) NOTED THAT THE ITALIAN 1976 CURRENT ACCOUNT WAS IN DEFICIT BY \$3 BILLION (RATHER THAN SECRETARIAT'S \$3-1/2 BILLION FIGURE) AND THAT THE GOVERN-

CONFIDENTIAL

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PAGE 01 OECD P 06420 05 OF 06 041255Z
ACTION EUR-12

INFO OCT-01 ISO-00 AID-05 CEA-01 CIAE-00 COME-00 EB-08
EA-07 FRB-03 INR-07 IO-13 NEA-10 NSAE-00 OPIC-03
SP-02 TRSE-00 LAB-04 SIL-01 AGRE-00 OMB-01 SSO-00
INRE-00 USIE-00 NSC-05 SS-15 STR-04 NSCE-00 EURE-00
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TO SECSTATE WASH DC IMMEDIATE 5575

INFO ALL OECD CAPITALS 0728

C O N F I D E N T I A L SECTION 05 OF 06 OECD PARIS 06420

MENT EXPECTS 1977 CURRENT ACCOUNT TO BE NEAR BALANCE (I.E., PLUS OR MINUS \$500 MILLION). WIDMAN STATED THAT US ESTIMATES OF DEFICIT ARE SLIGHTLY HIGHER THAN THE SECRETARIAT'S \$4.5 BILLION FIGURE--\$5 TO 6 BILLION. WOHLIN PRESENTED A NEW ESTIMATE FOR SWEDEN'S 1976 DEFICIT OF \$2-1/2 BILLION AND A PROJECTION OF \$3 BILLION DEFICIT FOR 1977, COMPARED WITH \$1-1/2 BILLION AND \$1-3/4 BILLION RESPECTIVELY IN SECRETARIAT'S TABLE.

14. CHAIRMAN OF TEMPORARY WORKING PARTY (VAN YPERSELE)

REPORTED ON CURRENT ACCOUNT AND FINANCING PROSPECTS FOR SMALLER OECD COUNTRIES BASED ON FEB. 25 MEETING OF WORKING PARTY. HE NOTED THAT 1976 DEFICIT FOR THESE COUNTRIES AS A GROUP WAS LARGER THAN HAD BEEN FORESEEN EARLIER AND THAT ONLY A SMALL REDUCTION IN THIS GROUP'S DEFICIT IS FORESEEN FOR 1977 (TABLE SUMMARIZING ESTIMATES BEING MAILED TREASURY/VAN BATENBURG). NO FINANCING PROBLEMS ARE EXPECTED FOR MOST OF THESE SMALLER COUNTRIES, BUT PORTUGAL AND TURKEY DO EXPECT SOME DIFFICULTIES THIS YEAR, AND SPAIN MAY PERHAPS ALSO FACE FINANCING DIFFICULTIES SOON. FINANCING PROBLEMS MAY SPREAD AS THESE COUNTRIES' DEFICITS CONTINUE INTO 1978 AND 1979, ALBEIT
CONFIDENTIAL

CONFIDENTIAL

PAGE 02 OECD P 06420 05 OF 06 041255Z

AT A SOMEWHAT LOWER LEVEL. (COMMENT: NOTING THAT SOME OF HIS REMARKS REPRESENTED PERSONAL VIEWS, VAN YPERSELEE PRESENTED A MORE PESSIMISTIC OUTLOOK RE FINANCING DIFFICULTIES THAN EMERGED FROM COUNTRIES' PRESENTATIONS AT THE TWP MEETING--SEE REF C.) WHILE INTERNAL ADJUSTMENT MEASURES, WITH EMPHASIS ON IMPROVING DOMESTIC DEMAND AND SUPPLY CONDITIONS, ARE APPROPRIATE FOR THESE COUNTRIES, SOME OF THEM FACE STRUCTURAL, SOCIAL AND POLITICAL LIMITS ON RESTRICTING INTERNAL DEMAND. STRENGTHENING OF DOMESTIC DEMAND BY COUNTRIES IN SURPLUS WOULD BE OF SOME HELP TO THESE COUNTRIES IN DEFICIT, AND FOR THOSE WHO WILL FACE DIFFICULTIES IN OBTAINING PRIVATE FINANCING, OFFICIAL FINANCING FACILITIES MAY BE NECESSARY.

15. IN HIS SUMMATION EMMINGER POINTED TO CONSIDERABLE PROGRESS TOWARD BETTER BALANCE IN INTRA-OECD CURRENT ACCOUNTS WHICH IS OCCURRING WITHRESPECT TO THE THREE LARGE DEFICIT COUNTRIES ON THE ONE HAND (COMINED DEFICIT DECLINING FROM \$11 BILLION TO \$4 BILLION IN 1977), AND THE SIX STRONGEST ON THE OTHER (COMBINED SURPLUS EXPECTED TO DECLINE FROM \$11 BILLION TO \$3.5 BILLION IN 1977). HE FELT THIS PROCESS COULD NOT BE ACCELERATED AND THAT FURTHER PROGRESS, WHILE LIKELY, WOULD TAKE SOME TIME. THE MAIN QUESTION IS THE CHOICE OF THE VARIOUS ADJUSTMENT INSTRUMENTS AVAILABLE (DEMAND MANAGEMENT, EXCHANGE RATE AND SELECTIVE POLICIES, THE LATTER CATEGORY INCLUDING ENERGY CONSERVATION AND AID POLICIES) AND HOW RESPONSIBILITY FOR USING THEM SHOULD BE ASSIGNED BETWEEN SURPLUS AND DEFICIT COUNTRIES. EMMINGER READ WITH APPROVAL IMF MANGAGING DIRECTOR WITTEVEEN'S PRINCIPLES FOR ADJUSTMEEN AS USED IN MANILA SPEECH AND REPEATED IN IMF DOCUMENT ID(77)2. THE STRONGEST COUNTRIES HAD INDICATED EXPECTATIONS OF CONSIDERABLE IMPORT GROWTH, ALTHOUGH HE NOTED SOME QUESTION AS TO HOW BENEFICIAL THIS WOULD BE FOR OTHER OECD COUNTRIES TO THE EXTENT THAT THE LARGER US DEFICIT MIGHT REFLECT GREATER OIL IMPORTS. NEVERTHE-

CONFIDENTIAL

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PAGE 03 OECD P 06420 05 OF 06 041255Z

LESS, HE SAW REASON FOR SOME OVERALL OPTIMISM, WHICH WAS BOLSTERED BY THE ABSENCE OF CONCERN ON THE PART OF THE MAJOR DEFICIT COUNTRIES REGARDING AVAILABILITY OF FINANCING. ON THE OTHER HAND, THE SIZE AND PERSISTENCE OF DEFICITS OF SMALLER OECD COUNTRIES WAS A MATTER OF SOME

CONFIDENTIAL

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PAGE 01 OECD P 06420 06 OF 06 041248Z

ACTION EUR-12

INFO OCT-01 ISO-00 AID-05 CEA-01 CIAE-00 COME-00 EB-08
EA-07 FRB-03 INR-07 IO-13 NEA-10 NSAE-00 OPIC-03
SP-02 TRSE-00 LAB-04 SIL-01 AGRE-00 OMB-01 SSO-00
INRE-00 USIE-00 NSC-05 SS-15 STR-04 NSCE-00 EURE-00
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O R 041140Z MAR 77

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INFO ALL OECD CAPITALS 0729

C O N F I D E N T I A L SECTION 06 OF 06 OECD PARIS 06420

CONCERN, AND THERE WERE SOME CASES WHERE THE FINANCING SITUATION MIGHT PROVE CRITICAL. EARLIER WITH RESPECT TO NON-OIL DEVELOPING COUNTRIES, EMMINGER HAD SEEN A MORE FAVORABLE FINANCING PATTERN OF THEIR JOINT CURRENT ACCOUNT DEFICITS (PERHAPS \$22-25 BILLION), SUGGESTING THAT NET PRIVATE LENDING MIGHT ONLY NEED TO AMOUNT TO HALF OF THE \$11 TO 12 BILLION LENT IN 1976 (CONSIDERING THAT THIS AMOUNT HAD PERMITTED LDC'S TO INCREASE RESERVES BY \$8 BILLION). THUS EMMINGER FELT THAT CURRENT SIGNS OF GREATER RELUCTANCE BY BANKS TO LEND TO NON-OIL LDC'S COULD BE REFLECTED IN LOWER LENDING IN 1977 WITHOUT UNDUE HARDSHIP. HOWEVER, WHILE THE OUTLOOK FOR LDC'S AS A GROUP MIGHT BE REASSURING, THERE WERE PROBLEMS FOR A FEW.

16. DATE FOR NEXT MEETING WAS LEFT OPEN. POSSIBILITY

OF SCHEDULING MEETING PRIOR TO APRIL 28-29 INTERIM
COMMITTEE MEETING IN WASHINGTON IS UNDER CONSIDERATION.
SINCE THE IMF MISSION WAS CURRENTLY IN ITALY, A DISCUS-
SION OF THE ITALIAN SITUATION THAT WAS SCHEDULED FOR
THIS MEETING OF THE WORKING PARTY WAS POSTPONED FOR A
FUTURE MEETING. THE WORK PROGRAM FOR WP3 WAS DISCUSSED
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PAGE 02 OECD P 06420 06 OF 06 041248Z

AT DINNER. TOPICS SUGGESTED FOR WP3 CONSIDERATION
INCLUDE: INTERNATIONAL LIQUIDITY; EXCHANGE RATE AS AN
INSTRUMENT OF ADJUSTMENT; AND CHANGES IN COMPETITIVENESS
AS PART OF ADJUSTMENT. (SECRETARIAT PAPER ON THIS
LATTER SUBJECT THAT WAS SCHEDULED TO BE DISTRIBUTED AT
THIS MEETING IS REPORTEDLY NEAR COMPLETION.)
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Message Attributes

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